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No. 76-1058

IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

CENTRAL ILLINOIS PUBLIC SERVICE COMPANY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ of Certiorari to the United States
Court of Appeals for the Seventh Circuit

BRIEF OF AMERICAN GAS ASSOCIATION, AS AMICUS CURIAE, IN SUPPORT OF PETITIONER

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The American Gas Association files this brief in support of the petitioner, pursuant to Rule 42. Counsel for all parties have consented to the filing of this brief and have been properly served.

INTEREST OF AMICUS CURIAE

The American Gas Association is the national trade association for approximately 300 member companies providing natural gas distribution and transmission services to 160 million consumers in all 50 states. These member companies serve approximately 93 percent of the 43 million homes, businesses and industrial facilities which use natural gas. The purpose of the Association is to further the development of the gas industry and its service of the public interest.

Like the petitioner, members of the Association have service responsibilities over transmission and distribution networks covering extensive geographical areas. In order to fulfill these responsibilities, their employees must be temporarily assigned to the field, away from normal work stations. In the instant case, the petitioner made meal reimbursements to employees so assigned, without regard to their level of compensation. Many members of the Association also have reimbursement programs because they have found that employees on travel status encounter conditions which contribute to greater fatigue and enhanced appetite, stimulating increased nutritional requirements which must be accommodated at unfamiliar facilities. Like the present case, these reimbursements do not represent payments for services performed by the employees; there is no correlation between the amount of the reimbursement and the compensation level of the recipient.

These reimbursements have traditionally been viewed as non-remunerative business disbursements. Member companies have relied upon the uniform approach of case law, together with rulings of the Internal Revenue Service, which have all recognized that reimbursements made for non-remunerative business purposes of the employer do not constitute wages subject to withholding. However, recent rulings by the Service, and the Seventh Circuit's decision in this case, set forth a new approach which, if affirmed by this Court, would reclassify a significant portion of these reimbursement payments as wages, without regard to their non-remunerative nature. This approach is not only contrary to the language of the withholding statutes and existing case law, but it also poses a significant threat to the administrative viability of member programs. In addition, the new standard is being asserted retroactively, thereby threatening the imposition of unwarranted, retroactive economic penalties upon many member companies, whenever the Service decides to reject judicial interpretations of the statutory definition of wages.

ARGUMENT

I. The Employer's Business Purpose for Employee Reimbursements Should Determine Their Non-Remunerative Nature.

Section 3402 of the Internal Revenue Code of 1954 imposes a duty upon an employer to withhold income taxes from "wages", a term defined in § 3401(a) as "* * * all remuneration * * * for services performed by an employee for his employer * * * *". Accordingly, the withholding issue turns upon whether an employer's reimbursements constitute additional remuneration for services, or are paid for a business purpose which is unrelated to compensating employees for their services. The issue arises in this case because the reimbursed expenses were incurred for meals, which are items of personal consumption. However, when meals are consumed in business circumstances dictated by the requirements of the employer (as in this case), reim-

bursement of their cost is obviously a business charge which does not represent remuneration for services.

Contrary to the government's position, this business character is not changed merely because, in computing taxable income of employees, a distinction is made between overnight and non-overnight business travel. All of the decided cases, except the holding below, have treated the employee's tax situation as irrelevant. The outcome of these cases has uniformly turned upon the employer's business purpose for making the reimbursement.

The Service's earliest recognition of this standard came in O.D. 514, 1920-2 C.B. 90. It held that supper money disbursements to employees performing voluntary overtime work did not constitute taxable income, or wages, because the payments were made for the convenience of the employer. The business purpose of the employer was again considered determinative in Rev. Rul. 190, 1953-2 C.B. 303, and Rev. Rul. 54-429, 1954-2 C.B. 53. Moreover, as recently as 1959, the Service, relying upon the employer's non-remunerative business purpose, ruled that per diem allowances for employees on temporary assignment to remote job sites were not wages during the first year of the assignment. Rev. Rul. 59-371, 1959-2 C.B. 236.

Judicial analysis of employer reimbursement programs has followed the same standard. In *Stubbs, Overbeck & Assoc.* v. *United States,* 445 F.2d 1442 (5th Cir. 1971), the sole issue was the validity of the one-year limitation contained in Rev. Rul. 59-371 on the non-remunerative nature of per diem payments. The court invalidated the one-year rule and held that per diem allowances continuing beyond one year were not wages where the employer still considered them to be

reimbursements for temporary expenses incurred in its business. The courts have consistently applied this business purpose standard in other circumstances, and found that disbursements for various employee expenses did not constitute remuneration for services. *Humble Oil & Refining Co.* v. *United States,* 442 F.2d 1362 (Ct. Cl. 1971), *Humble Pipe Line Co.* v. *United States,* 442 F.2d 1353 (Ct. Cl. 1971), *Allstate Insurance Co.* v. *United States,* 530 F.2d 378 (Ct. Cl. 1976), (reimbursements for indirect moving expenses); *Peoples Life Insurance Co.* v. *United States,* 373 F.2d 924 (Ct. Cl. 1967), *Acacia Mutual Life Insurance Co.* v. *United States,* 272 F. Supp. 188 (Ct. Cl. 1967), (payment of company convention expenses).

Most recently, in *Royster Co.* v. *United States,* 479 F.2d 387 (4th Cir. 1973), the Fourth Circuit held that noon meal reimbursements to traveling salesmen did not constitute wages. The court noted expressly that the reimbursements were made without regard to the compensation levels of the various employees. It also found that the program was motivated by the employer's business purpose of keeping its salesmen in the field, thereby reducing transportation costs.

The first departure from the business purpose standard occurred in Rev. Rul. 69-592, 1969-2 C.B. 193. In that ruling, the Service relied upon this Court's decision in *United States* v. *Correll,* 389 U.S. 299 (1967), which held that day travel meal expenses were not deductible by the employee under § 162(a)(2); the Service ruled that the payments for those expenses were wages unless it was reasonable to believe the employee's deductible expenses for the year would, in the aggregate, exceed total meal allowances and per diem payments. The Service recently applied the same standard in Rev. Rul. 76-453, 1976-47 I.R.B. 6, revoking Rev. Rul. 190

and Rev. Rul. 59-371. In that ruling the Service held that certain employee transportation expenses were not deductible by the employee and, accordingly, were wages when reimbursed by the employer.

The essence of these recent rulings, and the government's position here, is that (1) reimbursements create § 61 gross income, (2) taxable income is created if the employee is unable to deduct the expenditure, due to the rules of § 62 (adjusted gross income) and § 162 (business expenses), and (3) the existence of taxable income requires withholding. This approach has nothing to do with distinguishing between remunerative and non-remunerative reimbursements. Moreover, it has been explicitly rejected as a distortion of the requirement of § 3401(a) that the employer withhold taxes from "wages", defined as "remuneration for services performed by an employee for his employer". In *Stubbs, Overbeck & Assoc.* v. *United States,* 445 F.2d 1142, 1149 (5th Cir. 1971), involving the wage status of per diem payments, the court stated:

> * * * Whether or not payments were taxable to, or deductible by, the employee is immaterial with regard to whether they are subject to withholding by the employer * * * *

The Court went on to state that an employee may receive payments which are includable in his taxable income, because they constitute an economic gain, but are not "wages" as defined in § 3401(a). Likewise, the Court of Claims noted in *Humble Pipe Line Co.* v. *United States,* 442 F.2d 1353, 1356 (Ct. Cl. 1971), that "* * * the term 'wages' has a much narrower meaning than the term 'income' because wages are merely one form of income". This same principle has also been recognized in *Peoples Life Insurance Co.* v. *United States,* 373 F.2d 924, 932; *Allstate Insurance Co.* v.

United States, 530 F.2d 378, 383; *Humble Oil & Refining Co.* v. *United States,* 442 F.2d 1362, 1368; *Acacia Mutual Life Insurance Co.* v. *United States,* 272 F. Supp. 188, 195.

In this case, the government is attempting to make the concept of remuneration for services under § 3401(a) subordinate to the development of deduction rules under § 62 (adjusted gross income) and § 162 (business expenses). This approach has been rejected by the case authorities discussed above. In addition, such a result could hardly have been within the contemplation of Congress. Where deductibility has been considered material in withholding determinations, Congress has expressed itself clearly. *See* § 82, § 217, §3401(a)(15).

Moreover, the rule urged by the government would greatly disrupt the administration of per diem and flat-rate reimbursement programs. The business purpose of the reimbursement and the business reasons for the expense would be ignored. Instead, in determining their withholding obligations, employers would be required to treat each type of reimbursed expenditure separately and then analyze its deductibility to each individual employee. For example, with respect to per diem programs, an employer would have to extract and separately test each element of cost, thereby placing its withholding obligations in a state of confusion.

Only by viewing reimbursement programs from the standpoint of the business purpose of the employer can non-remunerative reimbursements be distinguished from wage compensation. Only this standard discloses the existence of a business purpose unrelated to remuneration for services, which is the essence of the definition of wages under § 3401(a).

II. Retroactive Imposition of a Withholding Tax Constitutes an Unjust Penalty When Failure to Withhold Was Consistent with Then Current Authority.

Since an employer is a mere collection agent for the government, it should not be subject to taxation under § 3403 until it has been clearly advised of its withholding obligations on the payments in question. For the tax year in issue (1963), the petitioner had no notice that meal money reimbursements might constitute wages. On the contrary, the petitioner, in reliance upon the business purpose standard, had reason to believe that its reimbursements were not wages. It was not until 1969 that the Service, in Rev. Rul. 69-592, departed from the business purpose standard for determining whether reimbursements are wages and first notified employers that meal money reimbursements might be subject to withholding. The petitioner, as well as other similarly situated taxpayers, should not be penalized for relying in good faith upon an established approach to the definition of wages, particularly when they had no notice in 1963 of a contrary government position.

The real issue in this case is not the liability of the petitioner under § 3403. The real issue in this case is the income tax liability of individual employees who received meal payments. However, no such liability has been asserted against these employees. Purely for administrative convenience, the government is attempting to collect these individual liabilities from a single source by retroactively redefining the term "wages". Unfortunately, the withholding structure creates a convenient vehicle for this type of abuse.

The government has attempted, without success, to accomplish similar results in earlier cases. In *Peoples*

Life Insurance Co. v. *United States,* 373 F.2d 924, 933 (Ct. Cl. 1967), the Court of Claims rejected the government's attempt to impose a withholding tax liability upon company convention expenses and observed that the withholding statute had not been intended "* * * as a device * * * to determine the basic tax liability of the employee, who (was) not even a party to the case". This theme was reiterated in *Humble Oil & Refining Co.* v. *United States,* 442 F.2d 1362, 1369 (Ct. Cl. 1971), where the court expressed concern that the Service had not given employers notice that reimbursements for indirect moving expenses would be considered wages.

With respect to moving expense reimbursements, Congress changed the law in order that reimbursed indirect moving expenses would come within the statutory definition of wages. *See* § 82, § 217 and § 3401(a)(15). Rather than seeking similar Congressional assistance in this situation, the government is now asking this Court to distort the statutory definition of wages —remuneration for services—to include the meal payments in issue.

CONCLUSION

The payments in issue should be governed by the statutory definition of wages interpreted in the context of the employer's business purpose. In that context, these payments do not fall within the statutory definition of wages, since they are not remuneration for services. In any event, the government should not be allowed to impose a withholding liability, on a retroactive basis, by asking this Court to adopt a new and

expanded interpretation of a clearly-stated statutory definition.

Respectfully submitted,

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